

Message Text

UNCLASSIFIED

PAGE 01 LONDON 08800 01 OF 05 121816Z

53

ACTION EB-11

INFO OCT-01 EUR-25 ISO-00 SP-03 AID-20 NSC-07 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03

PA-04 PRS-01 USIA-15 AEC-11 CIAE-00 COME-00 DODE-00

FEAE-00 FPC-01 INR-10 INT-08 NSAE-00 PM-07 SAM-01

SCI-06 DLOS-07 ACDA-19 FRB-02 CEQ-02 COA-02 EPA-04

IO-14 NSF-04 DRC-01 /226 W
----- 102659

R 121803Z JUL 74

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 2073

INFO USMISSION EC BRUSSELS

UNCLAS SECTION 01 OF 05 LONDON 08800

E.O. 11652: N/A

TAGS: ENRG, UK

SUBJECT: SEC STATE FOR ENERGY'S REPORT ON UNITED KINGDOM
OFFSHORE OIL AND GAS POLICY

REF: LONDON 8680, LONDON 8688

REFTELS REPORTED ON PROSPECTIVE ANNOUNCEMENT OF NEW HMG
POLICY TOWARD NORTH SEA OFFSHORE DEVELOPMENT AND AMBASSA-
DOR'S DISCUSSION WITH SEC STATE FOR ENERGY ERIC VARLEY.
FOLLOWING IS TEXT OF VARLEY'S REPORT TO PARLIAMENT
PRESENTED JULY 11:
"UNITED KINGDOM OFFSHORE OIL AND GAS POLICY"

BEGIN TEXT:

INTRODUCTION

THE LABOUR PARTY ELECTION MANIFESTO EXPRESSED "LABOUR'S
DETERMINATION TO ENSURE NOT ONLY THAT THE NORTH SEA AND
CELTIC SEA OIL AND GAS RESOURCES ARE IN FULL PUBLIC OWNER-
UNCLASSIFIED

UNCLASSIFIED

PAGE 02 LONDON 08800 01 OF 05 121816Z

SHIP, BUT THAT THE OPERATION OF GETTING AND DISTRIBUTING

THEM IS UNDER FULL GOVERNMENT CONTROL WITH MAJORITY PUBLIC PARTICIPATION". THE GOVERNMENT HAVE ALSO MADE IT CLEAR THAT IT IS THEIR INTENTION TO ENSURE THAT AS A RESULT OF THE EXPLOITATION OF THESE RESOURCES MAXIMUM BENEFIT IS CONFERRED ON THE COMMUNITY, AND PARTICULARLY ON SCOTLAND AND THE REGIONS ELSEWHERE WITHIN WHICH THE OLDER INDUSTRIAL REVOLUTION INDUSTRIES WERE DEVELOPED AND WHICH HAVE SUFFERED FOR A GENERATION FROM THE DECLINE OF THOSE INDUSTRIES. THIS PAPER CONTAINS THE GOVERNMENT'S PROPOSALS FOR ACHIEVING THESE OBJECTIVES.

2. BRITAIN'S OIL IS OF COURSE ALREADY PUBLICLY OWNED. PUBLIC OWNERSHIP WAS ESTABLISHED BY THE LAST CONSERVATIVE GOVERNMENT BUT ONE UNDER THE THE CONTINENTAL SHELF ACT 1964. IT WAS THEREFORE THE GOVERNMENT'S TASK TO WORK OUT A NEW STRUCTURE AND TAXATION ARRANGEMENTS WHICH WOULD COMBINE THEIR MANIFESTO COMMITMENT WITH AN ASSURANCE TO THE OIL COMPANIES ABOUT THE SUBSTANTIAL ROLE THAT WOULD REMAIN TO THEM.

THE REVIEW OF POLICY

3. ACCORDINGLY, IMMEDIATELY ON TAKING OFFICE THE GOVERNMENT BEGAN A FUNDAMENTAL REVIEW OF CONTINENTAL SHELF POLICY. THEY HAD VERY MUCH IN MIND THE EXCELLENT REPORT BY THE PUBLIC ACCOUNTS COMMITTEE UNDER THE THEN CHAIRMANSHIP OF THE PRESENT PAYMASTER GENERAL, AND THE MANY REPRESENTATIONS WHICH THEY HAVE RECEIVED FROM ALL INTERESTED PARTIES SINCE THEY CAME INTO OFFICE. THAT REVIEW IS NOW LARGELY COMPLETE. THIS PAPER SUMMARISES ITS CONCLUSIONS UNDER THREE HEADINGS: GOVERNMENT TAKE AND PARTICIPATION; CORPORATION TAX CHANGES; AND MEASURES TO HELP SCOTLAND AND OTHER DEVELOPMENT AREAS.

GOVERNMENT TAKE AND PARTICIPATION

4. THE GOVERNMENT PUBLISHED NEW FORECASTS OF OIL PRODUCTION IN MAY. THEY NOW EXPECT THE UNITED KINGDOM'S OIL PRODUCTION TO REACH 100 - 140M TONS IN 1980 AND 100 - 150M TONS A YEAR, OR EVEN MORE, THROUGHOUT THE 1980S. DURING THE PAST YEAR, THE WORLD PRICE OF OIL HAS MORE THAN QUADRUPLED; THE AVERAGE F.O.B. PRICE OF MIDDLE EASTERN OIL, A YEAR AGO ABOUT \$2 A BARREL, IS NOW \$9-10. IF PRICES REMAIN HIGH AND WITH THE HIGH PRODUCTION NOW EXPECTED, PROFITS ON OUR OFFSHORE OIL WILL BE ENORMOUS.

UNCLASSIFIED

UNCLASSIFIED

PAGE 03 LONDON 08800 01 OF 05 121816Z

IF THE CURRENT PRICE OF OIL CONTINUES, AND ON A REALISTIC ESTIMATE OF OUTPUT, ANNUAL PRE-TAX PROFITS WOULD TOTAL SOME 4,000 MILLION POUNDS BY 1980. UNDER PRESENT ARRANGEMENTS, TAX AND ROYALTY WOULD TAKE A RELATIVELY SMALL PROPORTION OF PROFITS IN THE EARLY YEARS, AND WOULD NEVER TAKE MUCH MORE THAN HALF. THE RESULT IS THAT NORTH SEA LICENSEES WOULD REAP ENORMOUS AND UNCOVENANTED PROFITS ON THEIR INVESTMENT. A HALF OR MORE OF THE POST-TAX

PROFITS ARE LIKELY TO BE REMITTED OVERSEAS; BY 1980 THE COST OF SUCH REMITTANCES TO OUR BALANCE OF PAYMENTS COULD UNDER PRESENT ARRANGEMENTS REACH, OR EVEN EXCEED 1,000 MILLION POUNDS ANNUALLY.

5. THIS SHOWS THAT AN INTOLERABLE SITUATION WOULD ARISE. PROMINENT LEADERS IN THE OIL INDUSTRY THEMSELVES ACCEPT THAT A MORE EQUITABLE ARRANGEMENT IS ESSENTIAL. IT ALSO SHOWS HOW MUCH IS AT STAKE IN DEVELOPING THIS MAJOR NATURAL RESOURCE FOR THE BENEFIT OF THE NATION. THIS IS WHAT THE GOVERNMENT INTEND TO DO. THEY HAVE TWO OBJEC-

UNCLASSIFIED

NNN

UNCLASSIFIED

PAGE 01 LONDON 08800 02 OF 05 121823Z

53

ACTION EB-11

INFO OCT-01 EUR-25 ISO-00 SP-03 AID-20 NSC-07 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03

PA-04 PRS-01 USIA-15 AEC-11 CIAE-00 COME-00 DODE-00

FEAE-00 FPC-01 INR-10 INT-08 NSAE-00 PM-07 SAM-01

SCI-06 DLOS-07 ACDA-19 FRB-02 CEQ-02 COA-02 EPA-04

IO-14 NSF-04 DRC-01 /226 W

----- 102754

R 121803Z JUL 74

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 2074

INFO USMISSION EC BRUSSELS

UNCLAS SECTION 02 OF 05 LONDON 08800

TIVES:

- TO SECURE A FAIRER SHARE OF PROFITS FOR THE NATION AND TO MAXIMISE THE GAIN TO THE BALANCE OF PAYMENTS. THIS MUST MEAN A BIG INCREASE IN GOVERNMENT REVENUE FROM THE CONTINENTAL SHELF. ON THE OTHER HAND, THE OIL COMPANIES MUST HAVE A SUITABLE RETURN ON THEIR CAPITAL INVESTMENT; THE GOVERNMENT RECOG-

NISE THAT THE COSTS OF EXPLORATION AND DEVELOPMENT
HAVE BEEN VERY HEAVY.

- TO ASSERT GREATER PUBLIC CONTROL; THIS IS ESSENTIAL
IF THE GOVERNMENT ARE TO SAFEGUARD THE NATIONAL
INTEREST IN AN IMPORTANT RESOURCE WHICH BELONGS TO
THE NATION.

TO ACHIEVE THESE OBJECTIVES, THE GOVERNMENT INTEND TO
TAKE ACTION UNDER FIVE HEADS:

FIRST, LEGISLATION WILL BE PROPOSED IN AN EARLY
FINANCE BILL TO IMPOSE AN ADDITIONAL TAX ON THE
COMPANIES' PROFITS FROM THE CONTINENTAL SHELF AND,
AS DESCRIBED IN THE FOLLOWING SECTION OF THIS PAPER,
UNCLASSIFIED

UNCLASSIFIED

PAGE 02 LONDON 08800 02 OF 05 121823Z

TO CLOSE VARIOUS LOOPHOLES IN THE RULES GOVERNING
EXISTING TAXATION ON THE COMPANIES' PROFITS.
SECONDLY, IT WILL BE MADE A CONDITION OF FUTURE
LICENSES THAT THE LICENSEES SHALL, IF THE GOVERNMENT
SO REQUIRE, GRANT MAJORITY PARTICIPATION TO THE
STATE IN ALL FIELDS DISCOVERED UNDER THOSE LICENSES.
THIS WILL BROADLY FOLLOW THE "CARRIED INTEREST"
PATTERN SUCCESSFULLY DEVELOPED IN NORWAY UNDER WHICH
THE STATE HAS AN OPTION TO ACQUIRE OWNERSHIP OF A
SPECIFIED PROPORTION OF OIL OR PROFITS, MEETING THE
SAME PROPORTION OF COSTS.

THIRDLY, IT IS THE GOVERNMENT'S BELIEF THAT MAJORITY
STATE PARTICIPATION IN THE EXISTING LICENSES FOR
COMMERCIAL FIELDS PROVIDES THE BEST MEANS FOR THE
NATION TO SHARE FULLY IN THE BENEFITS OF NORTH SEA
OIL WITHOUT UNFAIRNESS TO THE LICENSEES SINCE THE
STATE CONTRIBUTES ITS SHARE OF THE COSTS, INCLUDING
PAST COSTS. CERTAINLY THIS IS THE SOLUTION ADOPTED
WITH THE CONSENT OF THE OIL COMPANIES IN ALMOST EVERY
OTHER MAJOR OIL AND GAS PRODUCING COUNTRY IN THE
WORLD, NOT ONLY THOSE IN THE MIDDLE EAST. INDEED,
PUBLIC SECTOR PARTICIPATION HAS WORKED SUCCESSFULLY
IN THE BRITISH SHELF WITHOUT INJURY TO OIL COMPANY
INTERESTS THROUGH THE NATIONAL COAL BOARD AND
BRITISH GAS - WHOSE PRESENT SHARES WILL BE ACCEPTED
AS A SHARE IN THE TOTAL PUBLIC PARTICIPATION. THE
GOVERNMENT HOPE THAT THE COMPANIES WILL RECOGNISE
THE STRENGTH OF THEIR VIEWS ON THIS. THEY WANT THE
OIL COMPANIES TO CONTINUE TO INVEST IN THE NORTH SEA
ON PROFITABLE TERMS. THEY WILL BE VERY READY TO
LISTEN TO WHAT THE COMPANIES SAY AND CONSIDER WITH
THEM HOW THE COMMON INTEREST CAN BEST BE SERVED.
THEY ARE SURE THE INDUSTRY WILL WANT TO SUBMIT THEIR
VIEWS AT THE EARLIEST POSSIBLE MOMENT AND TO ENTER
INTO TALKS ON THIS BASIS. THE GOVERNMENT WILL BE
INVITING THEM TO DO SO SHORTLY.

FOURTHLY, A BRITISH NATIONAL OIL CORPORATION (BNOC) WILL BE SET UP, THROUGH WHICH THE GOVERNMENT WILL EXERCISE THEIR PARTICIPATION RIGHTS. THIS CORPORATION WILL REPRESENT THE GOVERNMENT IN THE PRESENT CONSORTIA (AND WILL TAKE OVER THE PRESENT INTERESTS
UNCLASSIFIED

UNCLASSIFIED

PAGE 03 LONDON 08800 02 OF 05 121823Z

OF THE NATIONAL COAL BOARD) AND ALSO BUILD UP A POWERFUL AND EXPERT SUPERVISORY STAFF THAT WILL EN-ABLE IT TO PLAY AN ACTIVE PART IN THE FUTURE DEVELOPMENT, EXPLORATION AND EXPLOITATION OF THE CONTINENTAL SHELF. IT WILL ALSO HAVE POWERS TO EXTEND ITS ACTIVITIES ULTIMATELY TO THE REFINING AND DISTRIBUTION OF OIL. THE HEADQUARTERS OF THE BNOC WILL BE IN SCOTLAND.

FIFTHLY, THE GOVERNMENT WILL EXTEND THEIR POWERS TO CONTROL PHYSICAL PRODUCTION AND PIPELINES. EXPERIENCE HAS SHOWN THAT THERE ARE MANY WEAKNESSES IN THE CURRENT SYSTEM. THE GOVERNMENT WILL, THEREFORE, FOR CURRENT AS WELL AS FUTURE LICENCES, TAKE POWER TO CONTROL THE LEVEL OF PRODUCTION IN THE NATIONAL INTEREST. THIS DOES NOT AFFECT THEIR DETERMINATION TO BUILD UP PRODUCTION AS QUICKLY AS POSSIBLE OVER THE NEXT FEW YEARS. THE QUESTION OF REDUCING THE RATE OF DEPLETION IS UNLIKELY TO ARISE FOR SOME YEARS BUT THE GOVERNMENT BELIEVE THAT THEY SHOULD TAKE THE NECESSARY POWERS NOW. THEY WILL ALSO TAKE POWERS TO RECEIVE ROYALTY IN KIND, AND TO REMIT ROYALTY IN CERTAIN CIRCUMSTANCES; TO CONTROL THE DEVELOPMENT OF UNDERSEA PIPELINES, IN THE SAME WAY AS ON LAND; TO

UNCLASSIFIED

NNN

UNCLASSIFIED

PAGE 01 LONDON 08800 03 OF 05 121825Z

53

ACTION EB-11

INFO OCT-01 EUR-25 ISO-00 SP-03 AID-20 NSC-07 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03

PA-04 PRS-01 USIA-15 AEC-11 CIAE-00 COME-00 DODE-00

FEAE-00 FPC-01 INR-10 INT-08 NSAE-00 PM-07 SAM-01

SCI-06 DLOS-07 ACDA-19 FRB-02 CEQ-02 COA-02 EPA-04

IO-14 NSF-04 DRC-01 /226 W

----- 102763

R 121803Z JUL 74

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 2075

INFO USMISSION EC BRUSSELS

UNCLAS SECTION 03 OF 05 LONDON 08800

INTRODUCE TIGHTER CONTROL OVER EXPLORATION AND DEVELOPMENT; AND TO REQUIRE LICENSEES TO PROVIDE MORE INFORMATION ABOUT THEIR ACTIVITIES THAN IS NOW OBLIGATORY. ALL THESE NEW PROPOSED POWERS, TOGETHER WITH EXISTING POWERS, WILL ENABLE THE GOVERNMENT ALSO TO ENSURE THAT DEVELOPMENT IS CARRIED OUT WITH PROPER CARE FOR THE ENVIRONMENT AND FOR THE PLANNING OF INFRASTRUCTURE. THE DETAILED IMPLEMENTATION OF THESE AND OTHER CHANGES WILL BE DISCUSSED WITH THE COMPANIES.

6. THE GOVERNMENT INTEND TO BRING LEGISLATION ON THESE MATTERS AND ON THE ESTABLISHMENT OF A BRITISH NATIONAL OIL CORPORATION BEFORE PARLIAMENT AS SOON AS POSSIBLE.

7. THERE ARE OTHER MATTERS WHICH ARE STILL BEING CONSIDERED, FOR EXAMPLE HOW THE NEW ARRANGEMENTS WILL APPLY TO GAS, ALTHOUGH IT IS ALREADY CLEAR THAT BRITISH GAS WILL HAVE A CONTINUING ROLE TO PLAY IN CONTINENTAL SHELF EXPLORATION AND PRODUCTION.

CORPORATION TAX CHANGES

UNCLASSIFIED

UNCLASSIFIED

PAGE 02 LONDON 08800 03 OF 05 121825Z

8. IN HIS BUDGET STATEMENT THE CHANCELLOR OF THE EX-CHEQUER MENTIONED VARIOUS LOOPHOLES IN THE EXISTING RULES GOVERNING TAXATION OF THE PROFITS OF THE OIL COMPANIES WHICH WERE DESCRIBED IN THE PUBLIC ACCOUNTS COMMITTEE REPORT ON NORTH SEA OIL AND GAS PUBLISHED ON 1 MARCH 1973 (HC 122). HE REFERRED FIRST TO THE PROPOSALS PUT FORWARD LAST YEAR BY THE PREVIOUS GOVERNMENT FOR DEALING WITH LOSSES WHICH HAVE ARISEN TO THE OIL COMPANIES FROM TRANSACTIONS IN OVERSEAS OIL AT ARTIFICIAL PRICES; AND SECOND, TO THE POINT MADE BY THE PUBLIC ACCOUNTS COMMITTEE IN RELATION TO THE GROUP RELIEF FOR CAPITAL ALLOWANCES ON INVESTMENT UNCONNECTED WITH THE NORTH SEA (HANSARD 26 MARCH

1974 COL. 320).

9. ON THE ARTIFICIAL LOSSES, THE GOVERNMENT'S OBJECTIVE, AS REGARDS THE COMPUTATION OF PROFITS FROM 1 JANUARY 1973, IS NO DOUBT THE SAME AS THAT OF THE PREVIOUS ADMINISTRATION; BUT IT IS PROPOSED TO ACHIEVE IT BY SOMEWHAT DIFFERENT MEANS FROM THOSE INDICATED LAST YEAR BY THE PREVIOUS CHANCELLOR. IT IS NOT PROPOSED THAT THE PRICE AT WHICH OIL IS TREATED AS CHANGING HANDS FOR TAX PURPOSES SHOULD BE DETERMINED BY THE PROCEDURE OF A FORMAL ADMINISTERED PRICE, SINCE THIS WOULD RAISE PRACTICAL DIFFICULTIES, PARTICULARLY IN THE CURRENT SITUATION OF THE OIL MARKET. INSTEAD IT IS PROPOSED TO STRENGTHEN THE EXISTING TRANSFER PRICING LEGISLATION IN SECTION 485 OF THE INCOME AND CORPORATION TAXES ACT 1970 SO THAT THE TRANSACTIONS IN QUESTION ARE BROUGHT SQUARELY WITHIN ITS SCOPE. IT IS ALSO PROPOSED TO INTRODUCE IN THAT PROVISION GUIDELINES FOR DETERMINING A REALISTIC ARM'S-LENGTH PRICE. CERTAIN FURTHER PROVISIONS WILL BE NEEDED TO MAKE THE LEGISLATION EFFECTIVE; IN PARTICULAR, POWERS FOR THE REVENUE TO OBTAIN INFORMATION. THESE PROVISIONS, AS THE CHANCELLOR SAID IN HIS BUDGET STATEMENT, WILL TAKE EFFECT FROM 1 JANUARY 1973.

10. NEXT THERE ARE LOSSES WHICH HAD ACCRUED TO THE OIL COMPANIES AT 31 DECEMBER 1972 - THAT IS, BEFORE THE NEW TRANSFER PRICING RULES TAKE EFFECT. THE PREVIOUS GOVERNMENT HAD PROPOSED THAT THESE LOSSES SHOULD BE SEGREGATED SO THAT THEY WERE SET ONLY AGAINST FUTURE PROFITS FROM THE EXISTING BUSINESS AND NOT AGAINST PROFITS FROM THE CONTINENTAL SHELF.

UNCLASSIFIED

UNCLASSIFIED

PAGE 03 LONDON 08800 03 OF 05 121825Z

11. THE GOVERNMENT HAVE GIVEN CAREFUL THOUGHT TO THIS QUESTION AND HAVE DECIDED THAT TO ALLOW THESE LOSSES TO GO FORWARD INDEFINITELY AGAINST PROFITS FROM EXISTING ACTIVITIES (OTHER THAN NORTH SEA ACTIVITIES) WOULD REPRESENT AN UNJUSTIFIABLE COST TO THE REVENUE. THE PURPOSE OF THE NEW TRANSFER PRICING PROPOSALS DESCRIBED ABOVE IS TO ENSURE THAT THE PROFITS OF THE DOWNSTREAM ACTIVITIES OF THE OIL GROUPS ARE COMPUTED ON A REALISTIC BASIS FOR TAX PURPOSES. THE EFFECT OF THIS WOULD BE LARGELY VITIATED, PERHAPS FOR YEARS TO COME, IF THE COMPANIES WERE ALLOWED TO REDUCE THEIR UNITED KINGDOM TAX LIABILITY ON THESE PROFITS TO NIL BY CARRYING FORWARD THE ARTIFICIAL LOSSES WHICH AROSE AS A RESULT OF THE USE OF ARTIFICIAL PRICES IN THE PAST. THOSE LOSSES DID NOT REPRESENT ANY REAL COMMERCIAL LOSS AND THERE IS THEREFORE NO EQUITABLE REASON WHY THEY SHOULD BE USED TO ELIMINATE FUTURE TAX LIABILITIES.

12. IT IS PROPOSED THEREFORE THAT THOSE LOSSES SHOULD BE CANCELLED FROM TODAY. CLEARLY THERE WOULD BE A CASE FOR

SAYING THAT THEY SHOULD BE CANCELLED FROM 1 JANUARY 1973.
NEVERTHELESS THE GOVERNMENT RECOGNISE THAT SINCE CANCELLA-
TION OF THE LOSSES GOES FURTHER THAN THE PROPOSALS PUT
FORWARD BY THE FOREMER ADMINISTRATION, THERE COULD BE
SAID TO BE AN ELEMENT OF RETROSPECTION, WITHOUT WARNING,

UNCLASSIFIED

NNN

UNCLASSIFIED

PAGE 01 LONDON 08800 04 OF 05 121826Z

53

ACTION EB-11

INFO OCT-01 EUR-25 ISO-00 SP-03 AID-20 NSC-07 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03

PA-04 PRS-01 USIA-15 AEC-11 CIAE-00 COME-00 DODE-00

FEAE-00 FPC-01 INR-10 INT-08 NSAE-00 PM-07 SAM-01

SCI-06 DRC-01 DLOS-07 ACDA-19 FRB-02 CEQ-02 COA-02

EPA-04 IO-14 NSF-04 /226 W

----- 102842

R 121803Z JUL 74

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 2076

INFO USMISSION EC BRUSSELS

UNCLAS SECTION 04 OF 05 LONDON 08800

IN APPLYING THE CANCELLATION FROM 1 JANUARY 1973. THE
LOSSES WILL THEREFORE BE AVAILABLE FOR CARRY FORWARD,
SUBJECT TO THE NORMAL RULES, AGAINST PROFITS (OTHER THAN
ANY NORTH SEA PROFITS) UP TO TODAY'S DATE. CORRESPONDING
LIMITATIONS WILL BE NECESSARY ON THE USE OF CAPITAL ALLOW-
ANCES FOR EXPENDITURE ALREADY INCURRED OUTSIDE THE UNITED
KINGDOM CONTINENTAL SHELF.

13. THE ALLOWANCE OF LOSSES AGAINST THE 1973 PROFITS AND
PART OF THE 1974 PROFITS WILL IN THE GOVERNMENT'S VIEW BE
SUFFICIENT IN GENERAL TO COPE WITH ANY POSSIBLE GENUINE
ELEMENT IN THE ACCUMULATED LOSSES. NEVERTHELESS, IN VIEW
OF THE UNCERTAINTY AT THE PRESENT TIME OF THE AMOUNT OF

THE COMPANIES' TAXABLE PROFITS FOR THESE YEARS, IT IS ALSO PROPOSED THAT EACH COMPANY SHALL BE ALLOWED TO CARRY FORWARD A MINIMUM OF 50 MILLION POUNDS OF ITS LOSSES, SO THAT IF THE SUM OF ITS TAXABLE PROFITS FOR 1973 AND FOR THE PERIOD FROM 1 JANUARY 1974 TO TODAY'S DATE IS LESS THAN 50 MILLION POUNDS IT WILL BE ENTITLED TO CARRY FORWARD THE BALANCE AGAINST PROFITS OF THE REST

UNCLASSIFIED

PAGE 02 LONDON 08800 04 OF 05 121826Z

OF 1974 AND OF SUBSEQUENT YEARS (EXCEPT ANY PROFITS ARISING FROM THE NORTH SEA).

14. NEXT, THERE IS THE QUESTION OF WHAT HAS COME TO BE CALLED A RING FENCE FOR THE NORTH SEA. THE LIKELIHOOD THAT THE CORPORATION TAX YIELD FROM THE NORTH SEA WOULD BE SUBSTANTIALLY REDUCED BECAUSE OF GROUP RELIEF FOR CAPITAL ALLOWANCES ON EXPENDITURE NOT CONCERNED WITH NORTH SEA PRODUCTION WAS VIEWED WITH CONCERN BY THE PUBLIC ACCOUNTS COMMITTEE. THE GOVERNMENT HAVE REVIEWED THIS VERY CAREFULLY, AND HAVE DECIDED THAT A RING FENCE IS ESSENTIAL TO PROTECT THE TAX YIELD FROM THE NORTH SEA. THIS WILL OF COURSE BE A DEPARTURE FROM THE NORMAL CORPORATION TAX RULES. WHATEVER VIEW MAY BE TAKEN OF THE GENERAL EFFECT OF THOSE RULES, HOWEVER, THERE IS NO DOUBT THAT THE NORTH SEA HAS CREATED AN ENTIRELY NEW SITUATION. EXCHEQUER RECEIPTS FROM THE NORTH SEA SHOULD NOT BE AT THE MERCY OF ALLOWANCES AND LOSSES RESULTING FROM EXTRANE-
OUS ACTIVITIES.

15. IT IS PROPOSED THEREFORE THAT GROUP RELIEF SHOULD NOT BE ALLOWABLE AGAINST PROFITS FROM NORTH SEA ACTIVITIES. CORRESPONDINGLY, THE NORTH SEA PROFITS OF A SINGLE COMPANY WITH OTHER ACTIVITIES WILL NOT BE REDUCED FOR TAX PURPOSES BY LOSSES OR ALLOWANCES ARISING FROM THOSE OTHER

ACTIVITIES. NOR WILL A COMPANY WITH LOSSES OR EXCESS ALLOWANCES BE ABLE TO USE THEM TO CLAIM PAYMENT OF THE IMPUTATION TAX CREDIT ON DIVIDENDS RECEIVED FROM A COMPANY WITHIN ITS GROUP AND PAID OUT OF NORTH SEA PROFITS. THE RING FENCE WILL APPLY TO ACCOUNTING PERIODS ENDING AFTER TODAY'S DATE.

16. THESE TAX PROPOSALS ARE NECESSARY IN THE GOVERNMENT'S VIEW IN ORDER TO ENSURE THAT IN FUTURE THE EXCHEQUER DERIVES A FAIR RECEIPT FROM THE PROFITS OF THE OIL INDUSTRY, WHICH BETWEEN 1965 AND THE PUBLIC ACCOUNTS COMMITTEE REPORT ON NORTH SEA OIL AND GAS PAID ONLY A NEGLIGIBLE AMOUNT OF UNITED KINGDOM TAX ON PROFITS. AT THE SAME TIME THE GOVERNMENT BELIEVE THAT THEY ARE FAIR TO THE INDUSTRY ITSELF.

SCOTLAND

UNCLASSIFIED

UNCLASSIFIED

PAGE 03 LONDON 08800 04 OF 05 121826Z

17. THE GOVERNMENT MADE IT CLEAR, IN THE GRACIOUS SPEECH FROM THE THRONE, THAT IT WAS THEIR INTENTION TO ENSURE THAT AS A RESULT OF THE EXPLOITATION OF NORTH SEA OIL AND GAS RESOURCES MAXIMUM BENEFIT IS CONFERRED ON THE COMMUNITY, AND PARTICULARLY IN SCOTLAND AND REGIONS ELSEWHERE IN NEED OF DEVELOPMENT. THE GOVERNMENT RE-AFFIRM THIS

UNCLASSIFIED

NNN

UNCLASSIFIED

PAGE 01 LONDON 08800 05 OF 05 121828Z

53

ACTION EB-11

INFO OCT-01 EUR-25 ISO-00 SP-03 AID-20 NSC-07 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03

PA-04 PRS-01 USIA-15 AEC-11 CIAE-00 COME-00 DODE-00

FEAE-00 FPC-01 INR-10 INT-08 NSAE-00 PM-07 SAM-01

SCI-06 DLOS-07 ACDA-19 FRB-02 CEQ-02 COA-02 EPA-04

IO-14 NSF-04 DRC-01 /226 W

----- 102837

R 121803Z JUL 74

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 2077

INFO USMISSION EC BRUSSELS

UNCLAS SECTION 05 OF 05 LONDON 08800

COMMITMENT AND HAVE REACHED A DECISION IN PRINCIPLE UPON AN IMPORTANT SPECIAL MEASURE DESIGNED TO BENEFIT SCOTLAND.

18. THE GOVERNMENT HAVE DECIDED TO SET UP A SCOTTISH DEVELOPMENT AGENCY, FINANCED BY THE UNITED KINGDOM EX-CHEQUER, TO STRENGTHEN, IN AN EFFECTIVE AND LASTING WAY,

THE INSTRUMENTS AVAILABLE FOR PROMOTING THE DEVELOPMENT OF SCOTLAND'S ECONOMY AND UNDERTAKING MAJOR ENVIRONMENTAL PROJECTS. THE AGENCY WILL BE RESPONSIBLE TO THE SECRETARY OF STATE FOR SCOTLAND.

19. THE PRECISE ORGANISATION, FUNCTIONS AND POWERS OF THE AGENCY ARE BEING WORKED OUT IN FULLER DETAIL AS RAPIDLY AS POSSIBLE. LEGISLATION WILL BE NEEDED.

WALES

20. AS OIL EXPLORATION DEVELOPS IN THE CELTIC SEA, SIMILAR ARRANGEMENTS TO THE SAME END WILL BE MADE FOR WALES IN WALES. THE NATURE OF THESE ARRANGEMENTS IS BEING WORKED OUT AS QUICKLY AS POSSIBLE. THE INTENTION WOULD BE NOT ONLY TO MAKE GOOD THE DEFICIENCIES OF YESTERDAY BUT TO ENSURE THAT THE OPPORTUNITIES FOR MODERN INDUSTRI-
UNCLASSIFIED

UNCLASSIFIED

PAGE 02 LONDON 08800 05 OF 05 121828Z

AL DEVELOPMENT DO NOT GIVE RISE TO FURTHER SOCIAL ECONOMIC AND ENVIRONMENTAL PROBLEMS.

21. THE SECRETARY OF STATE FOR WALES HAS ALREADY ANNOUNCED AN OIL ADVISORY COMMITTEE WHICH WILL MEET UNDER HIS CHAIRMANSHIP TO REVIEW THOSE ASPECTS OF CELTIC SEA OIL AND GAS DEVELOPMENT OF PARTICULAR INTEREST TO WALES, AND TO ADVISE ON SIGNIFICANT ISSUES WITHIN HIS OWN FIELD OF EXECUTIVE AND OVERSIGHT RESPONSIBILITIES.

CONCLUSION

22. THESE ARE COMPREHENSIVE AND FAR-REACHING PROPOSALS. THEY SHOW THE GOVERNMENT'S DETERMINATION TO ACT, AND ACT QUICKLY, TO ENSURE THAT THE NATION GET FULL BENEFIT FROM THE NEWLY-DISCOVERED WEALTH. THE OIL COMPANIES ARE FULLY AWARE THAT THE PRESENT SYSTEM COULD NOT CONTINUE. THE GOVERNMENT ARE CONFIDENT THAT THE OIL COMPANIES WILL BE READY TO JOIN IN WORKING OUT A NEW STRUCTURE WHICH THEY KNOW WILL BE DURABLE BECAUSE IT WILL BE ACCEPTED BY THE PEOPLE OF BRITAIN. THEY ARE CONFIDENT TOO THAT THE NEW STRUCTURE WILL BRING SUBSTANTIAL BENEFITS TO THE WHOLE COUNTRY, AND IN PARTICULAR TO THE REGIONS IN NEED OF DEVELOPMENT. END TEXT.

SOHM

UNCLASSIFIED

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: REPORTS, PETROLEUM, OFFSHORE OIL FIELDS, FOREIGN POLICY POSITION
Control Number: n/a
Copy: SINGLE
Draft Date: 12 JUL 1974
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Authority: n/a
Disposition Case Number: n/a
Disposition Comment:
Disposition Date: 01 JAN 1960
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1974LONDON08800
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D740187-0290
From: LONDON
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1974/newtext/t19740754/aaaabuad.tel
Line Count: 590
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EB
Original Classification: UNCLASSIFIED
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 11
Previous Channel Indicators: n/a
Previous Classification: n/a
Previous Handling Restrictions: n/a
Reference: LONDON 8680, LONDON 8688
Review Action: RELEASED, APPROVED
Review Authority: martinjw
Review Comment: n/a
Review Content Flags:
Review Date: 18 OCT 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <18 OCT 2002 by ThomasVJ>; APPROVED <16 JAN 2003 by martinjw>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: SEC STATE FOR ENERGY'S REPORT ON UNITED KINGDOM OFFSHORE OIL AND GAS POLICY
TAGS: ENRG, UK, (KISSINGER, HENRY A)
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005